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## *Topics for Discussion*

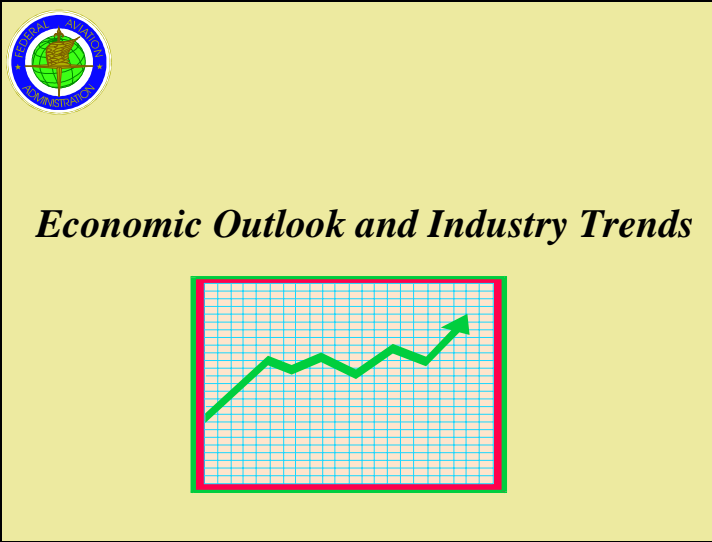
- **Review of 2000**
- **Economic Outlook and Industry Trends**
- **Aviation Perspectives**
- **Forecast Risks**



### *Review of 2000*

- **Domestic and International Traffic**
- **Air Carrier Finances**
- **General Aviation Activity**
- **Demand for FAA Services**

Traffic up for 9th consecutive year;  
Domestic RPMs up 6.3% - strong economy  
International RPMs up 6.8% - strong economy  
Regional RPMs up 18.2% - increased use of RJ's  
Cargo RTMs up 6.7% - International faster than domestic  
Industry profitable again in 2000.  
Revenues up 8.3% - Strong demand and higher yields  
Expenses up 10% - Higher fuel costs  
Total operating profits were \$7.6B.  
General Aviation indicators continue strong.  
Billings at all time high of \$8.2B- 250% higher than 1994  
Hours up 13% in 1999 - 5th consecutive year of increase  
Demand for FAA services continued to grow in 2000:  
Tower operations up 0.8%  
Instrument operations up 2.3%  
Center activity up 3.1%





***Factors Affecting Demand for  
and Supply of Air Carrier Services***

**Demand**

- Income
- Fares
- Tastes and preferences
- Demographics

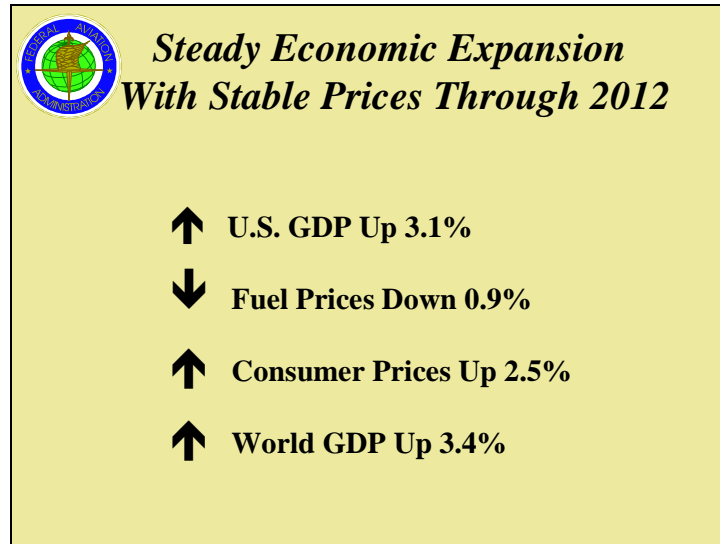
**Supply**

- Competition
- Restructuring
- Efficiency
- Fleet size

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## ***Demand Side Factors***

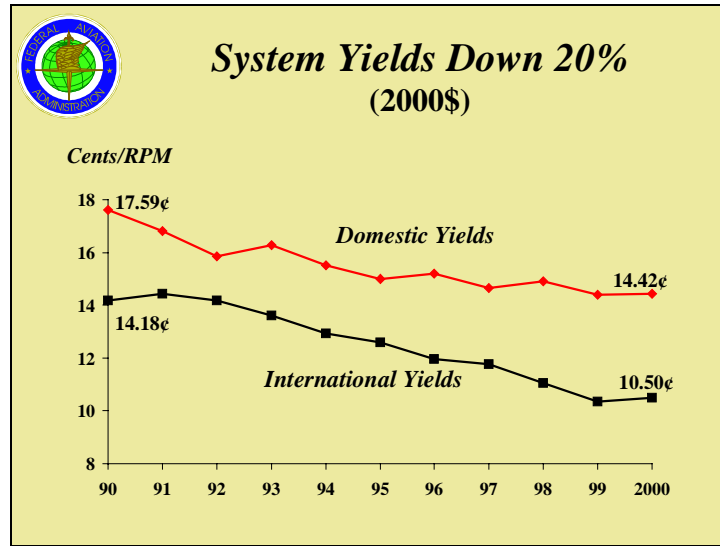


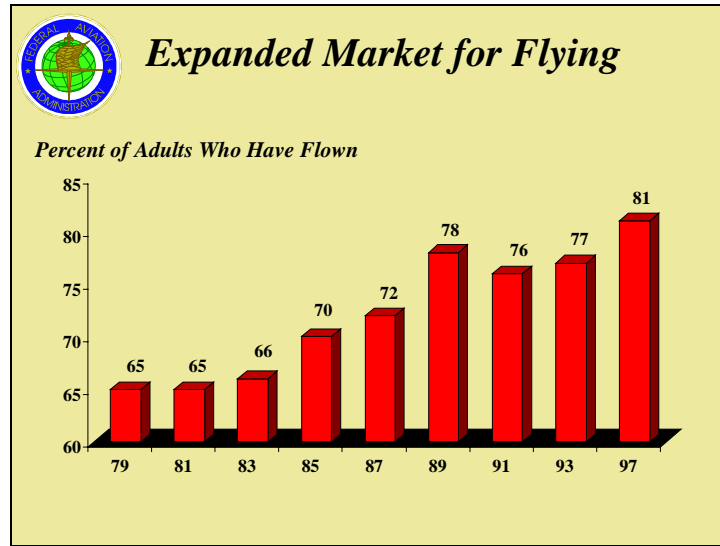
Comments here and for balance of speech reflect our latest outlook which is different than that published in the forecast book. The forecasts shown incorporate the latest OMB forecast which was released Jan 22, 2001.

The economic expansion, rapidly approaching its 11th year, is showing signs of coming to an end. OMB and the major forecasting services do expect U.S. economic growth to slow during the next few years, but not fall into recession.

Following an increase in the oil and gas index of 29.5% in 2000, the index is projected to decrease 5.0% in 2001 and then decline 21% over the next two years. Over the forecast period, real fuel prices fall about 3.4% a year. Following a rapid increase during the first half of the year, oil prices have fallen as the U.S. economy has slowed and OPEC has increased production. However, if the expected slowdown in the U.S. economy occurs during the next several years, oil production from non-OPEC countries increase, and one or more of the OPEC countries break ranks and increase production beyond OPEC quotas, we can expect slower growth of nominal fuel prices during the forecast period.










***Supply Side Factors***



### ***Low-cost Carrier Revolution***

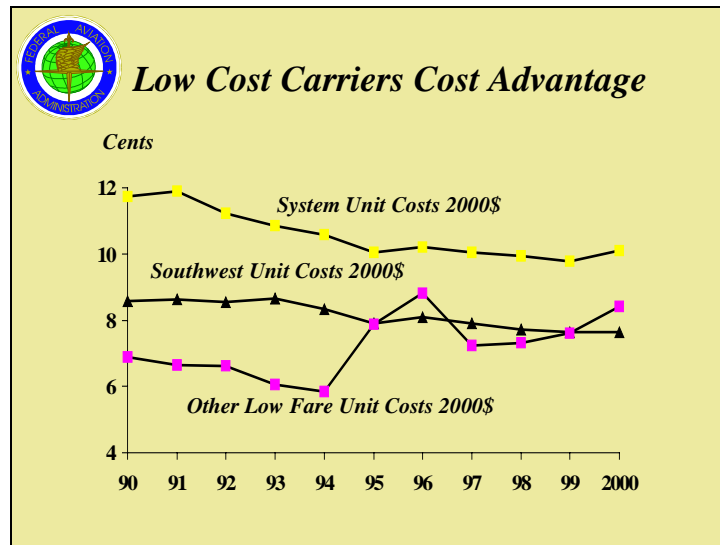
- **New entrants**
- **Southwest effect**
- **Two-tier carriers**

The second wave of expansion of low-cost, low-fare carriers during the 90s is having a major effect on efficiency, competition, the consumer, and industry structure. Today, about one in five passenger trips is on an airline that may be considered a low-fare operator. The monetary benefits for the consumer have been significant. A study by DOT showed that low-fare service saves consumers about \$6.3 billion annually. Although expansion of these carriers slowed following the crash of ValuJet flight in 1996, entry activity appears to be rebounding. During the past few years a number of low fare entrants (JetBlue and National in particular) have begun operations or expanded operations (AirTran, Frontier, Spirit) and been profitable.

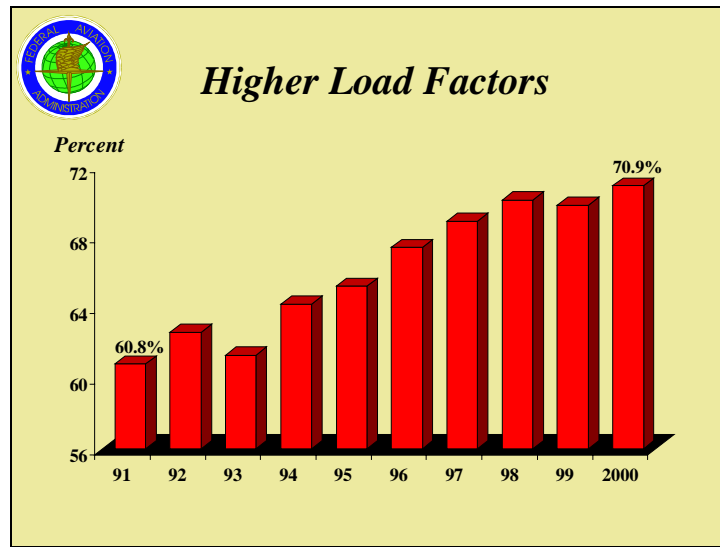
Southwest airlines with its highly efficient low-cost operation has successfully pursued a low-fare strategy in many secondary airport-pair markets. This strategy has played an important role in pushing down average fares and accelerating growth in traffic. In 160 short-haul markets that Southwest entered for the first time between 1990 and 1998, annual passenger traffic increased by more than 174% and real yields fell by 54%. Southwest now accounts for about 76% of the passenger traffic carried on low-fare airlines.

Southwest has provided the momentum for some major carriers to start low-cost, low-fare divisions such as US Airways MetroJet, Delta Express, and Shuttle by United. These second tier carriers have been put into markets as competitors for Southwest and other startup airlines.

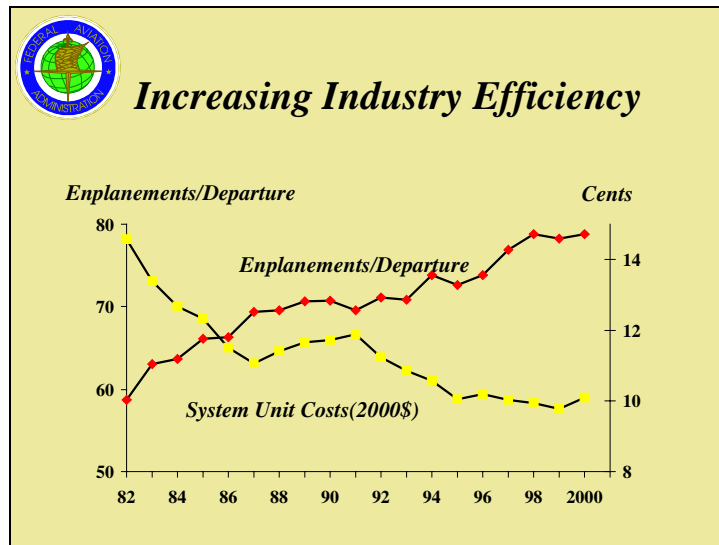
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In 2000 U.S. customers ordered 1,437 aircraft--the highest total ever. Regional Jets accounted for 45% (651 aircraft) of the orders.

Total orders placed during the four year period 1997 through 2000 (3,944) is greater than the number of orders placed during the prior 15 year period, 1982 through 1996.

In 1999 manufacturers delivered 519 jet aircraft to U.S. customers-- the largest number of deliveries on record.





## ***Redefining Regional Carriers***

**↑Expansion of regional jet fleet**

**↑Growing trip length**

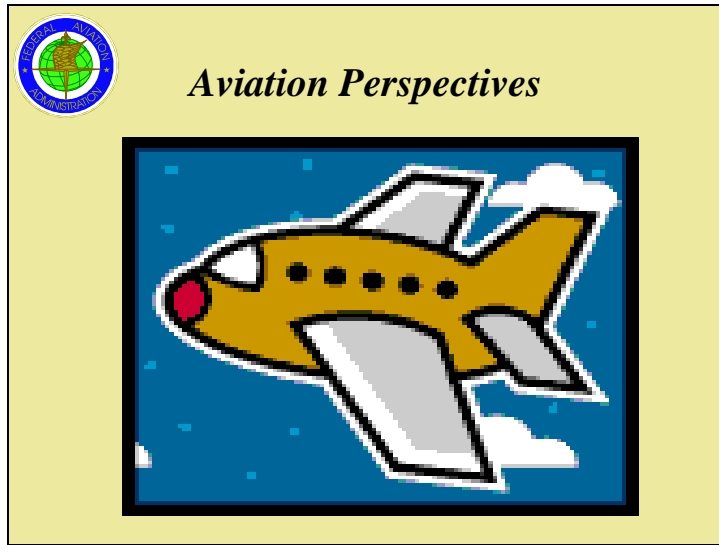
**↑Increasing aircraft size**

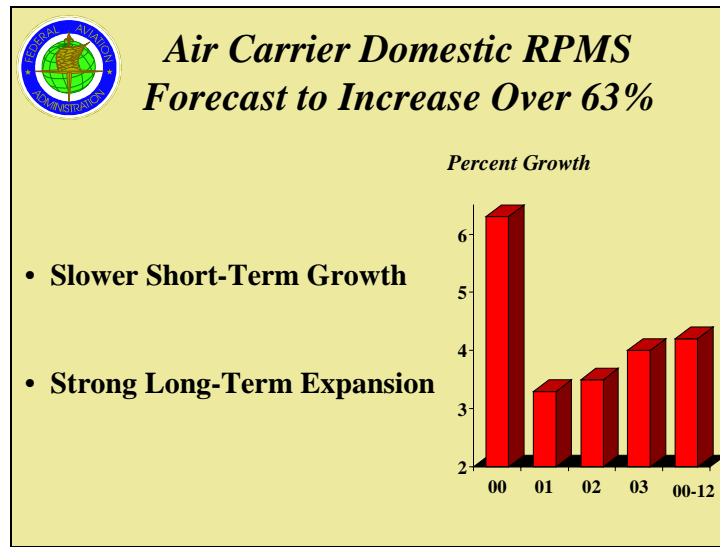
**↑Increasing load factors**



### ***Industry Forecast Assumptions***

- **Continued Economic Growth; no recession**
- **Intense competition remains**
- **Growing air carrier and regional fleets**
- **Stable load factors**
- **Increasing productivity**





Following an increase of 6.3% in 2000, commercial air carrier domestic RPMs are forecast to increase 3.3% in 2001, 3.5% in 2002 and 4.0% in 2003. The slower growth through this period is based on the expected slower growth for the economy coupled with flat real yields. Traffic growth is forecast to gradually increase over the balance of the forecast period as the economy returns to its long-term growth path and real yields resume declining at historic rates.

For the period 2000 through 2012, domestic RPMs are expected to increase 4.2% a year (OMB projects GDP to increase 3.1% a year through the period).

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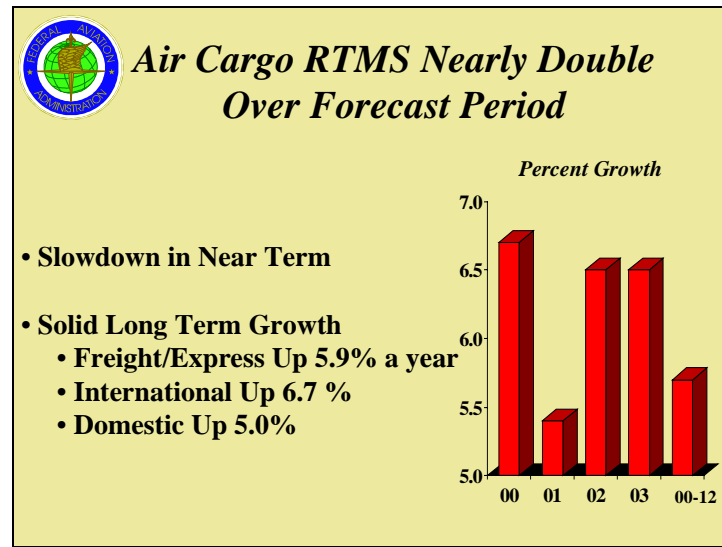


Traffic in international markets is projected to increase at rates above the domestic market.

Over the 12-year forecast period, total international passengers to and from the U.S. on both U.S. and foreign flag carriers are projected to increase almost 86%, expanding from 139 million in 2000 to 259 million in 2012.

The highest rates of growth are forecast for the Latin American and Pacific regions with annual growth of 6.4% and 6.2% respectively. The Atlantic market is expected to increase 4.4% annually over the forecast period.

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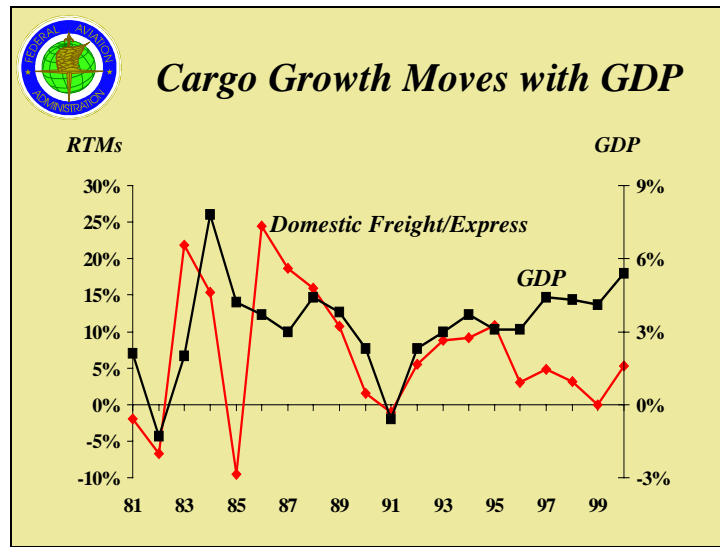


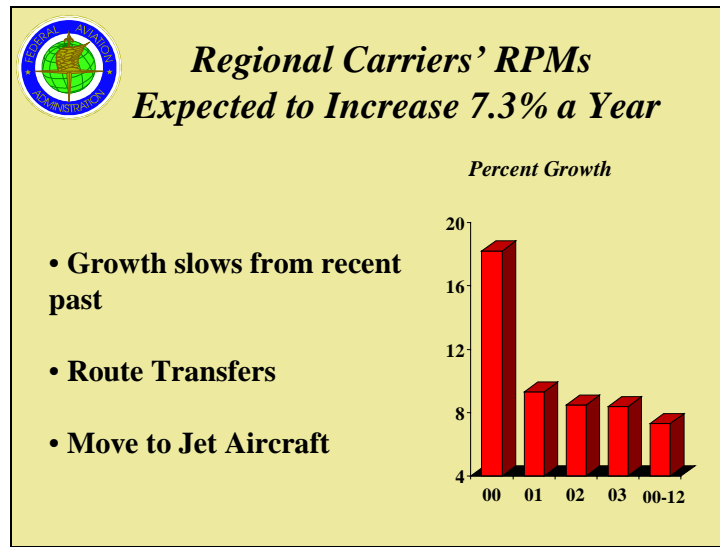
Total RTMs (freight/express and mail) are forecast to increase from 30.0 billion in 2000 to more than 58.5 billion in 2012--up 5.7% a year.

Growth in the short term is stronger driven by a robust international sector.

The relatively high growth in international freight/express RTMs is based upon expected strong economic growth in Latin America and the Asia/Pacific regions. Between 1991 and 1999 all-cargo carriers increased their share of international freight/express RTMs from 50.5% to 53.6%. Although the share fell sharply in 2000, the trend of increasing all-cargo carriers share is expected to continue throughout the forecast period, with all-cargo carriers share of international freight/express RTMs increasing to 60.3%.

To accommodate growth in air cargo, the cargo jet aircraft fleet is forecast to increase from 1,073 aircraft in 2000 to 1,760 aircraft in 2012.





Regional carrier RPMs increased 18.2% in 2000. Growth slows in 2001 to 9.3% and over the forecast period, RPMs are projected to more than double, expanding from 22.3 billion in 2000 to 52.2 billion in 2012.


The regional jet fleet is forecast to increase from 569 in 2000 to 2,190 in 2012.

Increased use of regional jets is expected to lead to expanded transfer of routes of the large commercial air carriers to their regional partners.

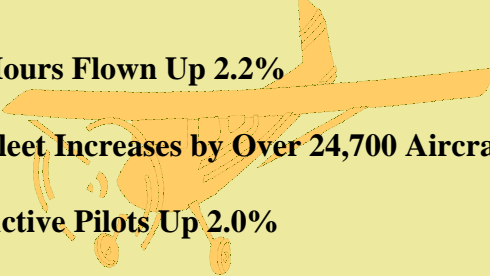
Regional jets with ranges up to 1,000 miles will open up growth opportunities in non-traditional markets.

Average aircraft size, trip length, and load factors are expected to show significant increases over the forecast period.





### ***Recovery of General Aviation Expected to Continue***

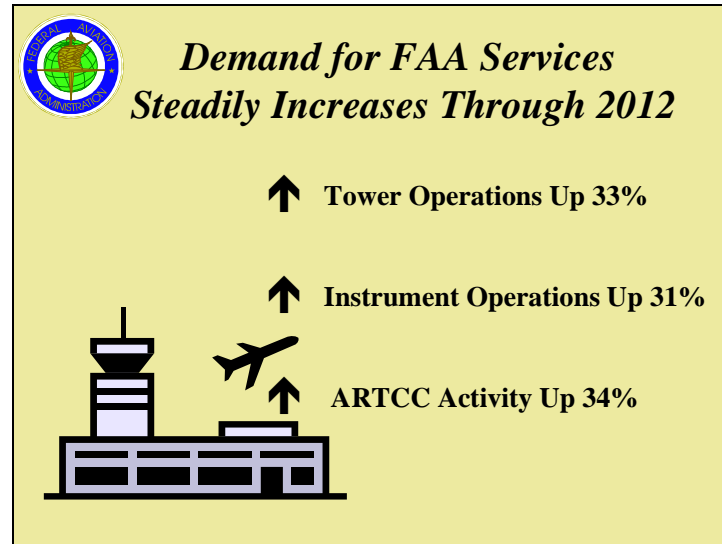


- ↑ Hours Flown Up 2.2%**
- ↑ Fleet Increases by Over 24,700 Aircraft**
- ↑ Active Pilots Up 2.0%**

In 2000 aircraft shipments increased 12.0%, while the total number of active general aviation and air taxi aircraft increased by 1,820.

Forecast growth in hours flown by general aviation of 2.2% a year is due to the expansion of the fleet over the forecast period by 24,752 aircraft and increased aircraft utilization. The turboprop/turbojet fleet is expected to show the largest increase over the 12-year forecast period, expanding 3.0% a year.

Largest growth in hours is expected in the turboprop/turbojet market--up 5.2% a year driven by the continuing rapid growth in fractional ownership and corporate jets.



Operations at combined FAA and contract towers are projected to increase 2.4% over the 12-year forecast period. Commercial aircraft activity is projected to grow 2.8% per year with air carrier activity increasing 3.0% per annum.

Growth in instrument operations slows from 2.3% in 2000 to 1.9% in 2001 due to the expected slowing of the economy then increase at a faster rate for the balance of the forecast. Instrument operations over the forecast period expand 2.2% a year with commercial activity growing 2.7% annually as air carrier activity increases 3.0% per year.

General aviation instrument operations, which increased only 1.0% a year during the 90s, are expected to increase 1.9% a year over the forecast period, primarily due to the relatively large growth in the fleet of the more sophisticated general aviation aircraft.

Growth in total IFR aircraft handled slows from 3.1% in 2000 to 1.9% in 2001. Over the forecast period IFR aircraft handled increases 2.5% a year.

General aviation aircraft handled at ARTCCs, which increased 1.3% a year during the 90s, is forecast to expand 1.9 percent a year through 2012.



### ***Forecast Risks***

- **Economic Slowdown/Recession**
- **Fuel prices**
- **ATC system capacity and delays**
- **Labor Issues**
- **Industry Consolidation**

One risk to our forecast is a slowdown in economic growth or even a recession. Recent data in the US has confirmed a pronounced slowdown in the economy and many forecasters are calling for a mild recession. Economic growth in other regions is slowing as well. Lack of a solid recovery in Japan is hurting Asia while Latin America is slowing down due to lower exports to the US.

Fuel prices constitute a second risk to our forecast. If fuel prices are higher than our forecast, the airline industry could be impacted in a number of ways: Lower profits, lower demand for air travel, lower capacity through increased retirements and exit of financially weaker carriers, and higher fares as fuel increases are passed on.

A third risk to the forecast is the amount of ATC system capacity available. Delays are growing along with traffic. Delays in 2000 were 20% higher than in 1999. The number of travelers impacted is significant. The DOT inspector general reported that for the first 9 months of 2000 “approximately 119 million passengers were delayed, canceled, or diverted.” Solutions to the problem in the form of additional runway capacity or modernization of the ATC system will not provide short term relief.

A fourth risk to the forecast is the rise in labor unrest. Rising labor unrest has resulted in operational disruptions and higher carrier costs. With a large number of contracts to be negotiated in the next few years, this constitutes one of the largest risks to the forecast.

A final risk to our forecast is the impact of industry consolidation. Consolidation is likely to lead to: higher fares, increased cost to the public due to operational disruptions, higher labor costs, and lower industry capacity.



## ***Forecast Summary***

- ↓ Slowing World Economic Growth**
- ↑ Expanding Capacity - Increasing Competition**
- ↑ Increasing Productivity and Falling Fares**
- ↑ Growing Air Travel Demand**
- ↑ Escalating Demand for FAA Services**